

# Securities Litigation Alert

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## National Defense Authorization Act Boosts SEC's Disgorgement Authority and Ability to Seek Other Equitable Relief

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### Amendments Come on the Heels of Supreme Court Decisions on SEC Disgorgement

On January 1, 2021, Congress passed the National Defense Authorization Act (NDAA). Embedded in the NDAA's more than 1,400 pages is Section 6501, containing significant amendments to Section 21(d) of the Securities Exchange Act of 1934 (the "Exchange Act"). These amendments address important aspects of the U.S. Securities and Exchange Commission's (SEC) ability to seek disgorgement and other equitable relief and follow two U.S. Supreme Court decisions—*Liu v. SEC*, 140 S. Ct. 1936 (2020) and *Kokesh v. SEC*, 137 S. Ct. 1635 (2017)—which each had cabined the SEC's disgorgement authority in several respects. See [here](#) and [here](#).

First, Section 21(d), as amended, grants the SEC explicit authority to seek disgorgement and the federal courts express authority to order disgorgement "[i]n any action or proceeding brought by the Commission under any provision of the securities laws."<sup>1</sup> The amendments empower the SEC to seek "disgorgement . . . of any unjust enrichment by the person who received such unjust enrichment" in civil actions.<sup>2</sup> Section 6501 also extends the statute of limitations for disgorgement and other equitable relief in certain cases. In particular, Section 6501 applies a 10-year statute of limitations period to scienter-based violations, including violations of Section 10(b) of the Exchange Act, Section 17(a)(1) of the Securities Act of 1933 and Section 206(1) of the Investment Advisers Act of 1940.<sup>3</sup> This 10-year statute of limitations also applies to other equitable remedies within the SEC's authority such as injunctions, bars, suspensions and cease-and-desist orders, whether or not the underlying securities law violation is scienter-based.<sup>4</sup> The amendments, however, affirm the five-year limitations period to seek disgorgement for nonscienter-based securities law violations. In addition, Section 6501 tolls the disgorgement and equitable relief statutes of limitations for periods of time during which a defendant is outside the United States.<sup>5</sup>

Further, these amendments are applicable to "any [SEC] action or proceeding that is pending on, or commenced on or after" the date of the NDAA's enactment.<sup>6</sup>

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Finally, the amendments do not address several elements of the *Liu* decision, including that the amount disgorged may not exceed the wrongdoer's net profits and disgorgement must be obtained for the benefit of investors. As a result, the federal courts will have to unpack how *Liu* will be applied in these respects to SEC disgorgement claims.

## SEC's Approach to Disgorgement Moving Forward

Combined with a transition to a new SEC Chair,<sup>7</sup> parties facing SEC investigations likely will encounter an immediate impact of the amendments on the SEC's approach to seeking disgorgement. With a 10-year statute of limitations for disgorgement for securities fraud violations, where applicable, parties may face protracted SEC investigations as the SEC staff attempts to establish more substantial disgorgement amounts. If the SEC staff decides to extend investigations for that purpose, parties should consider carefully how they respond to, and negotiate, SEC requests for tolling agreements. The SEC staff may also be tempted to expand its theories of securities fraud violations in order to leverage the 10-year statute of limitations for purposes of obtaining disgorgement over a longer period of alleged misconduct. Finally, with the benefit of a 10-year statute of limitations, the SEC staff may be reluctant to settle to nonscienter-based charges, for example, under Sections 17(a)(2) and (3) of the Exchange Act, without parties agreeing to a larger disgorgement amount in exchange for the SEC dropping scienter-based charges.

<sup>1</sup> NDAA § 6501(a)(3).

<sup>2</sup> *Id.* § 6501(a)(1)(B).

<sup>3</sup> *Id.* § 6501(a)(3).

<sup>4</sup> *Id.*

<sup>5</sup> *Id.*

<sup>6</sup> *Id.* § 6501(b).

<sup>7</sup> See [https://www.wsj.com/articles/bidens-candidate-for-sec-chairman-is-expected-to-be-tough-on-companies-11611743403?st=j00vwqvpctidwhc&reflink=desktopwebshare\\_permalink](https://www.wsj.com/articles/bidens-candidate-for-sec-chairman-is-expected-to-be-tough-on-companies-11611743403?st=j00vwqvpctidwhc&reflink=desktopwebshare_permalink).

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